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Professor Erhard's Address to OECD

Minister for Economic Affairs

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Enclosure No. 1
Despatch No.
From Bonn
May

THE WHOLE OF EUROPE IS OF IRREVERSIBLE VALUE TO ALL OF US

The Federal Republic Minister of Economics comments on the OEEC annual report - the economic problems of Europe.

During its 11th Ordinary Session in Strasbourg April 20 - 27, 1959, the Consultative Assembly of the Council of Europe, *inter alia*, dealt with the 10th Annual Report of OEEC. On this occasion, the present Chairman of the OEEC Council of Ministers, West Germany's Vice Chancellor and Federal Minister of Economics, Dr. Ludwig Erhard, made a speech of fundamental significance, in the course of which he dealt with Europe's economic problems and with the cooperation in the various European organizations.

Erhard began to comment on the OEEC report by pointing out that, economically, Europe is facing two vital issues today—one being the question of what needs to be done now after six European countries have created a common market, and negotiations on a multilateral and non-discriminating association between the six and the rest of the West European powers have no doubt suffered a regrettable setback. The apparent political importance of this problem, Erhard said, is the urgent task of finding fruitful solutions for it. The second big problem, he continued, is to find out what principles Europe could follow and what means would be appropriate to ensure an untroubled development of its economic growth which would not only enrich and promote its own potential prosperity, but also the welfare of material status of the underdeveloped parts of the world.

Dr. Erhard warned against a repetition of the mistakes which had been made in Europe during the boom period 1953-57 and added that today Europe is experiencing the beginning of a new economic expansion. In expecting a new growth of demand, one should prevent the economic revival from degenerating into an inflationary trend with its difficulties regarding the individual balances of payments, as had been the case during the previous boom period. Dr. Erhard continued that OEEC has been endeavoring to profit by the mistakes Europe had made, and the 10th Annual Report under review contained the guiding principles to be followed to permit a new future expansion to develop without stagflation.

Further Erhard went on to say that, although Europe had not succeeded during the past few years in filling the appropriate place in world economy, encouraging aspects were, nevertheless, noticeable. Dr. Erhard declared, "Even though some of the methods we have been employing did not come up to expectations, they still helped to obtain far better results both in respect to an expansion of production and a stability of prices than we know from a disquieting past. For instance, almost all of the countries, with a few exceptions, succeeded in restoring more or less the equilibrium of their balance of payments without having to resort to quantitative import restrictions. Productivity and improvement of the standard of living have been rather remarkable in comparison with the growth in the United States. It speaks well for Europe's will to establish orderly conditions that the boom was stopped before it could cause a serious crisis which would have destroyed

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confidence all around and, in the event of even more limited interference, could have brought about a deflation. However, the subsequent period of adjustment was short and mild."

Position and Position Factors

As another positive factor, Richard continued, one could regard the fact that the recession in the United States about a year ago had no prejudicial or prejudicial effects on European economy. It was true, Richard said, that exports to the United States had decreased slightly; however, there had been no crisis in public confidence which would have resulted in movements of capital. "On the contrary, the notorious dollar gap which had been so troublesome for us until a few years ago no longer exists, and if the European governments manage to avoid inflationary developments, i.e., an unsatisfied demand for goods, we need not worry about the future. By virtue of the relative strength of their foreign exchange position, most of the governments of the member states have made their currencies widely convertible, at least for foreigners, and some of them have extended even further in respect to a liberalization of the dollar. Nevertheless, I think that more should and could be done in this field."

However, the balance sheet of European economy, the Vice Chancellor went on to say, also has its negative points, and he offered as examples that endeavors to ensure a steady economic growth without attendant inflationary symptoms have not been fully successful. In most countries, Richard contended, the boom was accompanied by advancing prices. "Obviously, the measures many countries had taken in respect to monetary restrictions during the initial stage of inflationary trends were not strict enough. On the other hand, these countries were anxious later on to pursue an isolating currency policy as an end in itself, while ignoring at the same time other means of achieving stabilization such as an active tax policy. The striking success of the economic measures taken in France at the turn of the year (as a matter of fact, these measures conform absolutely to the recommendations which OEEC already and emphatically had been voicing in the past) shows that many of the difficulties that had cropped up could have been avoided had the European governments cooperated more closely."

Convertibility - General Example

However, one should not underestimate the success of all the efforts toward the coordination of the economic policy of the member countries within the framework of the OEEC. Professor Richard called the introduction of convertibility at the end of 1956 positive evidence of the efficacy of coordination between the European nations. "This event constitutes the crowning of protected and toll-free efforts toward complete liberation of international trade and payment transactions from artificial restrictions. Moreover, convertibility implies complete and, in a certain way, irreversible integration of European economy in the wider framework of world economy. For years I have been one of the staunchest supporters of free trade and convertibility of the currencies, and that is

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why I was particularly happy that convertibility could, contrary to all expectations, be realized earlier than timid pessimists had anticipated. I believe that the introduction of convertibility and the careful preparation of this step is one of the best examples of international cooperation."

The demands resulting from convertibility were presented by the Vice Chancellor in the following manner: "Convertibility and higher integration springing therefrom inevitably demands, along with increasing interdependency of the European national economies, a more stringent and careful coordination of the economic and trade cycle policy of the member countries. What we need is a true European 'trade cycle policy.' It appears to me that the OEEC, especially because of its broad basis, is the proper institution to enable us to arrive at directives of a generally binding character for such a policy. Yes, we shall have to investigate in what way we must extend and improve its organs which are called upon within the framework of that institution to assume the responsibility for mutual advice and the coordination of the economic policy. As it is, the current examination, or review, of the economic situation of the member countries already forms part of the work of the organization. In many instances, the OEEC has directed very exact recommendations to individual member countries. Therefore, I am convinced that the living tradition of daily cooperation in numerous practical and concrete problems of economic policy within the organization will produce an excellent basis for a vigorous promotion of future efforts. I am of the opinion that the recommendations made to the member countries perhaps should be still more concrete and specific in the future, and that we should investigate still more carefully and effectively to see if such recommendations are actually followed."

"International coordination of economic policy is, as indicated before, all the more efficacious, the more comprehensive the scope. That is why, in my opinion, it is of the greatest importance that in the future we should be able to count upon the cooperation of our American and Canadian friends within the framework of the OEEC. Even if they are not full members of the organization, nevertheless, they participate fully in its activity; we may derive benefit from their experiences, advice and interpretations of government policy and its aims."

The Most Urgent Task

Professor Lihard made the following remarks in reference to the most recent developments, the present situation, and the tendencies toward expansion: "It is the most urgent and clearly recognizable task of European economic policy to ensure with increased strength and efforts a general and consolidated economic growth. Toward the end of 1957 a fairly perceptible stagnation of the demand set in. At the same time, however, when the aptitude of Europe in the direction of further growth threatened to slacken, its balance of payments situation gained strength. Today, there is practically no country in Europe which has to struggle with financial difficulties. Above all, a declining demand and doubts in the continuity of a lasting expansion of production have contributed substantially to a relaxation of tension on the labor market. These factors, along with a

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recession of import prices, had a beneficial effect on price policy. Today we may state with satisfaction that the tendencies toward increased prices in 1958 could be parried in all countries and that even price cuts could avert themselves in wide domains.

"Due to this changed situation, in the summer of 1958, the Council of Ministers of the OEEC recommended to the governments of the member countries to follow from now on a policy aiming at the promotion of permanent economic progress. Most of the governments have taken steps in this direction. Among other things, for instance, the terms for borrowing were relaxed, and in some countries measures were even initiated for the promotion of expansion by way of the public budgets.

"There is no doubt that we have at the moment in many sectors of European economy substantial unused capacities. Since the foreign exchange reserves generally have reached a high level, and the situation on the labor markets may be regarded as tense in many places, there still should be scope for further expansion. Although we can hardly speak any longer of an investment boom in general, nevertheless, investment activities are still rather strong. The production plants have been modernized and their efficiency improved so that, in my opinion, a further increase in productivity can be expected in numerous countries as soon as new, expansive forces have been released."

On the Threshold of New Expansion

"In general, one may say that Europe is on the threshold of a new expansion which, eventually, we hope will be free from inflation. This potential power also may help those industries which temporarily fell into difficulties—the coal, steel, and textile industries. However, the general upward trend is still limited, and, therefore, we must watch carefully and continuously to see if the noticeable upward trends are actually strong enough to help a strong expansion to victory.

"Based on the experiences of the past years, the OEEC has set forth certain ideas in its annual report which, in my opinion, could serve as the framework for a policy of healthy economic growth in the near future. Quite correctly, it emphasizes that measures aiming at an expansion should not be the kind which increase demand and, in turn, result in inflation or in the imbalance of the balance of payments. It is the task of a well comprehended economic policy to prevent extreme distortions both upward and downward in production and employment and to ensure a healthy growth on a stable basis by instituting specific measures at the proper time. The authors of the report show especially the dangers arising out of an artificially increased overall demand.

"In the coming months, when further steps will be taken everywhere to promote expansion, one should bear in mind that, in view of past years' expansion of production capacity, the possibilities of expanding consumption should be used primarily. This recommendation does not mean that maintaining a high standard of investment activities might lose significance. Given a situation, however, in which production capacity of many branches of the economy is not used fully, a

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policy occasionally directed toward expansion of consumption is one of the instruments of a 'curbed' expansion. I am sure that I am not overemphasizing the interpretation of this thesis.

"I have already mentioned the difficulty of closer coordination, especially in view of the introduction of convertibility. This is no doubt one of the most urgent problems the OEEC will have to deal with in the near future.

"In this connection it is emphasized repeatedly that those countries which have an economically stronger position bear considerable responsibility for guaranteeing a steady economic growth. It cannot be denied, I believe, that the budget presented by the British Government a short time ago represents such effective contribution for handling an expansion which will, in view of the importance of this country, reflect to third markets. Economic activity in my own country in general can be considered satisfactory. Numerous symptoms point to a further increase of the expansion during the next months. Finally, we very expect American economy to continue in its upward trend."

Handling Unemployment "Cost Inflation"

Professor Ehard called the prevention of "cost inflation" a primary prerequisite to healthy economic growth. "In the OEEC report, attention is called to the danger of excessive wage and salary demands as the cause of inflationary development. Of course, increased productivity should be reflected also in higher working income. However, wage demands have to be adapted to the actual demand and cost conditions of the total economy. If a continued rise in the price level is to be prevented, one must see to it that higher productivity is also reflected in the reduction of prices."

Ehard referred again to the problem of the Free Trade Area and to the negotiations and relations between those European countries which belong to the Common Market and their neighbors which do not. He said, "The importance of continued discussions and endeavors for reconciliation cannot be evaluated highly enough for the economic future of Europe. In my opinion, it would be highly disastrous if the present insecurity regarding eventual results of negotiations would last any longer and if the kind of future arrangements which are to lead to an association of the Six with the Eleven are not clarified. In the interest of all of Europe, a solution must soon be found which guarantees comprehensive cooperation in the field of economic and social policy. The economic relations between the European countries during the last 10 years are characterized by the closeness of solidarity. A free Western Europe split in economic blocs or even reverted to bilateralism would be far weaker, politically as well as economically, than that which we have endeavored to build up since OEEC and the Council of Europe started their pioneer activities."

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We Stand Up For Europe!

Subsequent to the analysis of the OEEC annual report, Minister Erhard went on to say:

"To the material content of the report I want to add that, in my opinion, Europe's historical mission should not be considered as materialistic pursuits or a striving for political power. In view of the political menace to our old continent, we have to keep in mind that we cannot prosper unless we stick together. In the economic field we serve that purpose through OEEC. We should not and must not overlook, however, that European strength of mind and spirit stems particularly from its manifold ways of life. Individuality is the thing to immunize us against communism and collectivism and the totalitarian principles.

"I profess adherence to the objectives and aims of the Common Market and to its closer ties and mutual obligations. However, while the Common Market must not split Europe, I frankly state, with reference to OEEC, that all countries abiding by that organization should particularly endeavor to find more liberalized forms and mutually binding patterns of cooperation. The whole of Europe is a precious thing not to be lost to all of us.

"Personally, I believe we should not revert to the sins of the past. I have no intention of establishing analogies to the critical situation of the Thirties; however, that crisis was not some curse inflicted by heaven, but developed from beginnings. At that time the international tenet was that the ominous developments could be remedied effectively by the nationalistic and protectionistic policy of isolationists. Such dismantling of international economy turned out to be an infliction.

"Moreover, there were these wild notions that cartel arrangements might eliminate discrepancies between supply and demand. Instead of relaxing the existing tensions through volume-increasing trends and other means of encouraging consumption, one endeavored to re-establish the economic equilibrium by tampering with production, adjusting it to consumption which simultaneously decreased the national income. Of course, these efforts which were bound to fail meant disaster. Therefore, it is imperative at this date to halt these no-better-the-second-time practices. We must never forget that nationalism and egotism were the very scourges of Europe.

"We are standing up for Europe. Of course, we have learned a lot from the past the easy and the hard way, but dealing with the current situation we must be cognisant of our intrinsic responsibility. We know how to shape our common fortune, may our will to do the right and proper thing be strong and unlagging."

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